State of Arizona House of Representatives Forty-sixth Legislature First Regular Session 2003

CHAPTER 242

### **HOUSE BILL 2152**

#### AN ACT

AMENDING SECTIONS 20-167, 20-1098, 20-1098.01, 20-1098.03 AND 20-1098.04, ARIZONA REVISED STATUTES; RENUMBERING SECTIONS 20-1098.05 THROUGH 20-1098.15, ARIZONA REVISED STATUTES, AS SECTIONS 20-1098.07 THROUGH 20-1098.17, RESPECTIVELY; AMENDING TITLE 20, CHAPTER 4, ARTICLE 14, ARIZONA REVISED STATUTES, BY ADDING SECTIONS 20-1098.05 AND 20-1098.06; AMENDING SECTIONS 20-1098.07, 20-1098.08, 20-1098.09, 20-1098.10, 20-1098.13 AND 20-1098.15, ARIZONA REVISED STATUTES, AS RENUMBERED BY THIS ACT; AMENDING TITLE 20, CHAPTER 4, ARTICLE 14, ARIZONA REVISED STATUTES, BY ADDING SECTION 20-1098.18; RELATING TO CAPTIVE INSURERS.

(TEXT OF BILL BEGINS ON NEXT PAGE)

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1	Domestic stock life insurers,				
2	domestic stock disability				
3	insurers or domestic stock				
4	life and disability insurers		750.00	2.	250.00
5	Domestic life reinsurers,				
6	domestic disability reinsurers				
7	or domestic life and disability				
8	reinsurers	\$2	,250.00	\$5.	500.00
9	Mechanical reimbursement reinsurers		,250.00		500.00
10	All other insurers	_	70.00	• •	205.00
11	3. Certificate of registration as an				200.00
12	administrator or application for				
13	renewal under section 20-485.12	\$	100.00	\$	295.00
14	4. Authority to solicit applications	•	100100	•	233.00
15	for and issue policies by means				
16	of mechanical vending machines	\$	30.00	\$	90.00
17	5. Service company permit	Š	150.00	\$	450.00
18	6. Application for motor vehicle	•	130.00	•	430.00
19	service contract program approval	\$	150.00	¢	450.00
20	7. Life care contract application	•	130.00	•	430.00
21	or annual report	\$	225.00	ŧ	675.00
22	8. Filing annual statement	•	150.00	•	450.00
23	9. Annual statement filing for		130.00		430.00
24	exempt insurer transacting life				
25	insurance, disability insurance				
26	or annuity business pursuant to				
27	section 20-401.05		CE 00		100.00
28	10. Licenses and examinations:	\$	65.00	•	100.00
29	(a) Licenses:				
30					
31	Surplus lines broker's license, biennially		200 00		000 00
32	· · · · · · · · · · · · · · · · · · ·		300.00		900.00
33	All other licenses, biennially (b) Examinations for license:		30.00		90.00
34	(b) Examinations for license: Examination on laws and one kind				
35			0.00		
36	of insurance		8.00		25.00
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	more kinds of insurance 11. Miscellaneous:		15.00		45.00
38 39					
40	Fee accompanying service of		0.00		
	process upon director	\$	8.00	\$	25.00
41	Certificate of director,		1 55		
42	under seal		1.50		5.00
43	Copy of document filed in				_
44	director's office, per page		0.50		0.75

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- B. EXCEPT AS PROVIDED IN SECTION 20-1098.18, the director shall deposit, pursuant to sections 35-146 and 35-147, all fees collected pursuant to this section in the state general fund. A refund is not allowed for any unused portion of a fee, and the director shall not prorate fees.
- C. The license fees prescribed by this section shall be payment in full of all demands for all state, county, district and municipal license fees, license taxes, business privilege taxes and business privilege fees and charges of every kind.
- D. Each domestic stock life or disability insurer that pays the renewal fee required under subsection A of this section is entitled to a credit in the amount of at least four hundred fifty-five dollars but not more than six hundred eighty dollars, as adjusted pursuant to subsection F of this section, to apply to the premium tax the insurer then owes pursuant to section 20-224, but the credit is not cumulative.
- E. The director may contract for the examination for the licensing of adjusters, insurance producers, bail bond agents, risk management consultants and surplus lines brokers. If the director does so, the fee for examinations for licenses pursuant to this section is payable directly to the contractor by the applicant for examination. The director may agree to a reasonable examination fee to be charged by the contractor. The fee may exceed the amounts prescribed in this section.
- Each December 1, if the revenue collected from fees during the prior fiscal year is less than ninety-five per cent or more than one hundred ten per cent of the appropriated budget for the current fiscal year, the director shall revise all fees within the limits prescribed by subsection A of this section on a uniform percentage basis among all fee categories and shall adjust the credit prescribed by subsection D of this section as necessary in order to retain any required uniformity. The director shall revise the fees in such a manner that the revenue derived from the fees during the subsequent fiscal year equals at least ninety-five per cent but not more than one hundred ten per cent of the appropriated budget for the current fiscal year. The revised fee schedule shall be effective July 1 of the subsequent fiscal year. For the purposes of this subsection, appropriated budget does not include any appropriation for the operation of the captive insurance program established under chapter 4, article 14 of this title. Any fees collected from captive insurers pursuant to subsection H of this section shall not be counted for the purpose of meeting the requirement of this section to recover at least ninety-five but not more than one hundred ten per cent of the department's appropriated budget.
- G. The director may contract with a voluntary domestic organization of surplus lines brokers to perform any transaction prescribed in chapter 2, article 5 of this title, including the acceptance or maintenance of the reports required by section 20-408. The director may allow the contractor to charge a stamping fee. The surplus lines broker shall pay the stamping fee established pursuant to this section directly to the contractor.

- 3 -

- H. Captive insurers shall pay certificate of authority issuance and renewal fees as prescribed by the director.
- I. For the purposes of subsection G of this section, "stamping fee" means a reasonable filing fee charged by a contractor for any transaction prescribed in chapter 2, article 5 of this title, including the acceptance or maintenance of the reports required by section 20-408.
  - Sec. 2. Section 20-1098, Arizona Revised Statutes, is amended to read: 20-1098. <u>Definitions</u>

In this article, unless the context otherwise requires:

- 1. "Affiliate" has the same meaning prescribed in section 20-481.
- 2. "AGENCY CAPTIVE INSURER" MEANS A CAPTIVE INSURER THAT IS OWNED BY ONE OR MORE BUSINESS ENTITIES THAT ARE LICENSED IN ANY STATE AS INSURANCE PRODUCERS OR MANAGING GENERAL AGENTS AND THAT ONLY INSURE RISKS ON POLICIES PLACED THROUGH THEIR OWNERS.
- 2. 3. "Association" means any lawfully formed association of individuals, corporations, OR partnerships THAT HAS BEEN IN EXISTENCE FOR AT LEAST ONE YEAR AND THAT IS ORGANIZED FOR A PRIMARY PURPOSE OTHER THAN INSURING ITS MEMBERS. or associations that directly or collectively through its member organizations either:
- (a) Owns, controls or holds with power to vote all the outstanding voting securities of an association captive insurer that is incorporated as a stock insurer.
- (b) Possesses one hundred per cent voting control over an association captive insurer that is incorporated as a mutual insurer.
- 3. "Association captive insurer" means an insurer that insures risks of the member organizations of the association or the member organizations' affiliates.
- 4. "BUSINESS ENTITY" HAS THE SAME MEANING PRESCRIBED IN SECTION 20-281.
- 4. 5. "Captive insurer" means any pure captive insurer, or association AGENCY CAPTIVE INSURER, GROUP captive insurer OR PROTECTED CELL CAPTIVE INSURER that is domiciled in this state and that is formed and licensed under this article.
- 5. 6. "Controlled unaffiliated business" means a company that satisfies all of the following:
- (a) Is not an affiliate of the captive insurer providing coverage or reinsurance.
- (b) Has an existing contractual relationship with an affiliate of the captive insurer providing coverage or reinsurance out of which the subject risk of loss arises.
- (c) Whose risk management function is controlled by an affiliate of the captive insurer providing coverage or reinsurance.

- 4 -

- 7. "GROUP" MEANS EITHER:
- (a) A RISK RETENTION GROUP FORMED PURSUANT TO SECTION 20-2402 AND EITHER THE PRODUCT LIABILITY RISK RETENTION ACT OF 1981 (15 UNITED STATES CODE SECTION 3901) OR THE LIABILITY RISK RETENTION ACT OF 1986 (P.L. 99-563).
- (b) AN INDUSTRY GROUP OR ASSOCIATION THAT DIRECTLY OR THROUGH ITS MEMBERS SATISFIES AT LEAST ONE OF THE FOLLOWING CRITERIA:
- (i) OWNS OR CONTROLS, OR HOLDS WITH POWER TO VOTE, ALL OUTSTANDING VOTING SECURITIES OF A GROUP CAPTIVE INSURER INCORPORATED AS A STOCK INSURER.
- (ii) HAS COMPLETE VOTING CONTROL OVER A GROUP CAPTIVE INSURER INCORPORATED AS A MUTUAL INSURER.
- (iii) CONSTITUTES ALL OF THE SUBSCRIBERS OF A GROUP CAPTIVE INSURER FORMED AS A RECIPROCAL INSURER.
- 8. "GROUP CAPTIVE INSURER" MEANS A CAPTIVE INSURER THAT INSURES ONLY THE RISKS OF THE GROUP MEMBERS AND THEIR AFFILIATES.
- 9. "INDUSTRY GROUP" MEANS TWO OR MORE INDIVIDUALS OR BUSINESS ENTITIES THAT EACH:
- (a) PROCURE THE INSURANCE OF ANY RISK OR RISKS BY USE OF THE SERVICES OF A FULL-TIME EMPLOYEE ACTING AS AN INSURANCE MANAGER OR BUYER.
- (b) HAVE AGGREGATE ANNUAL PREMIUMS FOR INSURANCE ON ALL RISKS THAT TOTAL AT LEAST TWENTY-FIVE THOUSAND DOLLARS.
  - (c) HAVE AT LEAST TWENTY-FIVE FULL-TIME EQUIVALENT EMPLOYEES.
- 6. 10. "Manager" means a person who is experienced in the field of captive insurance and who maintains all documents relating to a captive insurer's operations, transactions and affairs in this state and assists the captive insurer in its management and compliance with this article.
- 7. "Member organization" means any individual, corporation, partnership, limited liability company or association that belongs to an association.
- 11. "PARTICIPANT" MEANS AN ENTITY AND ANY AFFILIATES OF THE ENTITY THAT ARE INSURED BY A PROTECTED CELL CAPTIVE INSURER PURSUANT TO A PARTICIPANT CONTRACT.
- 12. "PARTICIPANT CONTRACT" MEANS A CONTRACT BY WHICH A PROTECTED CELL CAPTIVE INSURER INSURES A PARTICIPANT'S RISKS AND LIMITS THE PARTICIPANT'S LOSSES TO THE ASSETS OF THE PROTECTED CELL.
- 13. "PROTECTED CELL" MEANS A SEPARATE ACCOUNT ESTABLISHED AND MAINTAINED BY A PROTECTED CELL CAPTIVE INSURER FOR ONE PARTICIPANT.
  - 14. "PROTECTED CELL CAPTIVE INSURER" MEANS A CAPTIVE INSURER:
- (a) IN WHICH THE MINIMUM CAPITAL AND SURPLUS REQUIRED BY APPLICABLE LAW IS PROVIDED BY ONE OR MORE SPONSORS.
  - (b) THAT IS FORMED AND LICENSED UNDER THIS ARTICLE.
- (c) THAT INSURES THE RISKS OF SEPARATE PARTICIPANTS THROUGH A CONTRACT.
- (d) THAT SEGREGATES EACH PARTICIPANT'S LIABILITY THROUGH ONE OR MORE PROTECTED CELLS.

- 5 -

- 8. 15. "Pure captive insurer" means any company that insures risks of its affiliate or controlled unaffiliated business.
- 16. "SPONSOR" MEANS AN ENTITY THAT MEETS THE REQUIREMENTS OF SECTION 20-1098.06 AND THAT THE DIRECTOR HAS APPROVED TO PROVIDE ALL OR PART OF THE CAPITAL AND SURPLUS REQUIRED BY APPLICABLE LAW TO OPERATE A PROTECTED CELL CAPTIVE INSURER.
- Sec. 3. Section 20-1098.01, Arizona Revised Statutes, is amended to read:

#### 20-1098.01. Licensing; authority

- A. If allowed by its articles of incorporation, bylaws or other organizational document, a captive insurer may apply to the director for a license to transact any insurance, except that:
- 1. A pure captive insurer shall not insure risks other than those THE risks of its affiliates or controlled unaffiliated business.
- 2. An association A GROUP captive insurer shall not insure risks other than those THE risks of the member organizations of its association and the organizations. ITS GROUP MEMBERS AND THE MEMBERS' affiliates.
  - 3. AN AGENCY CAPTIVE INSURER SHALL NOT:
  - (a) INSURE ANY RISKS OTHER THAN THOSE PLACED BY OR THROUGH ITS OWNERS.
  - (b) ENGAGE IN THE DIRECT WRITING OF LIFE OR DISABILITY INSURANCE.
- 4. A PROTECTED CELL CAPTIVE INSURER SHALL NOT INSURE ANY RISKS OTHER THAN THOSE OF ITS PARTICIPANTS.
- 3. 5. IN ADDITION TO ANY OTHER APPLICABLE RESTRICTIONS, a captive insurer shall not engage in THE DIRECT WRITING OF any of the following types of insurance business:
- (a) Hospital service corporations, medical service corporations, dental service corporations, optometric service corporations or hospital, medical, dental and optometric service corporations as defined in section 20-822.
  - (b) Health care services organizations as defined in section 20-1051.
  - (c) Prepaid dental plan organizations as defined in section 20-1001.
  - (d) Prepaid legal insurance contracts as defined in section 20-1097.
  - (e) Business of title insurance as defined in section 20-1562.
- (f) Personal motor vehicle or homeowner's insurance coverage or any component of that insurance coverage.
- (g) Direct writing of Commercial motor vehicle insurance policies unless the insured affiliate qualifies as a self-insurer pursuant to section 28-4007. This subdivision does not limit a captive reinsurer's ability to reinsure commercial motor vehicle insurance OR SUBSTANTIALLY SIMILAR SELF-INSURANCE REQUIREMENTS OF ANOTHER STATE.
- (h) Direct writing of Mortgage guaranty insurance as defined in section 20-1541.
- (i) Direct writing of Workers' compensation or employers' liability insurance policies. This subdivision does not limit a captive insurer's ability to reinsure workers' compensation or employers' liability insurance

- 6 -

EXCEPT IN CONNECTION WITH A SELF-INSURANCE PROGRAM AS PRESCRIBED IN SUBSECTIONS B AND C OF THIS SECTION.

- 4. 6. NOTHING IN PARAGRAPH 5 OF THIS SUBSECTION PROHIBITS A CAPTIVE INSURER FROM ACCEPTING REINSURANCE. A captive insurer shall not accept or cede reinsurance except as provided in section 20-1098.09 20-1098.11.
- 5. 7. A captive insurer that writes life insurance or disability insurance shall comply with all applicable state and federal laws.
- B. A PURE CAPTIVE INSURER MAY PROVIDE DIRECT COVERAGE OF WORKERS' COMPENSATION IN THIS STATE IF THE WORKERS' COMPENSATION COVERAGE IS PROVIDED UNDER A SELF-INSURANCE PROGRAM APPROVED BY THE INDUSTRIAL COMMISSION OF ARIZONA UNDER SECTION 23-961. A CAPTIVE INSURANCE PROGRAM AUTHORIZED BY SECTION 23-961 IS SUBJECT TO AND SHALL COMPLY WITH ALL REQUIREMENTS OF TITLE 23, CHAPTER 6, APPLICABLE TO SELF-INSURANCE.
- C. A PURE CAPTIVE INSURER MAY PROVIDE DIRECT COVERAGE OF WORKERS' COMPENSATION OR EMPLOYERS' LIABILITY INSURANCE IN ANOTHER STATE IN CONNECTION WITH A SELF-INSURANCE PROGRAM THAT IS QUALIFIED AS A SELF-INSURANCE PROGRAM UNDER THE APPLICABLE STATE OR FEDERAL LAW, AS DETERMINED BY THE AGENCY OR OTHER ENTITY THAT HAS JURISDICTION OVER THE SELF-INSURANCE PROGRAM.
- 8. D. A captive insurer shall not transact insurance business in this state unless:
- 1. It first obtains from the director a license authorizing it to transact captive insurance business in this state.
- 2. Its board of directors OR, FOR RECIPROCAL INSURERS, ITS SUBSCRIBERS ADVISORY COMMITTEE, holds at least one meeting each year in this state.
  - 3. It maintains its principal place of business in this state.
- 4. It appoints a resident statutory agent to accept service of process and to otherwise act on its behalf in this state and files the appointment with the director. In the case of a captive insurer formed as a corporation OR RECIPROCAL INSURER, if the statutory agent cannot with reasonable diligence be found at the registered office of the captive insurer, the director is an agent of the captive insurer on whom any process, notice or demand may be served.
- C. E. Before receiving a license, a captive insurer shall file with the director THE FOLLOWING:
- 1. IF FORMED AS A CORPORATION, a certified copy of its articles of incorporation, bylaws or other organizational document, a statement under oath of its president and secretary showing its financial condition and any other statement or document required by the director.
- 2. IF FORMED AS A RECIPROCAL INSURER, A CERTIFIED COPY OF THE POWER OF ATTORNEY OF ITS ATTORNEY-IN-FACT, A CERTIFIED COPY OF ITS SUBSCRIBERS' AGREEMENT, A STATEMENT UNDER OATH OF ITS ATTORNEY-IN-FACT SHOWING ITS FINANCIAL CONDITION AND ANY OTHER STATEMENT OR DOCUMENT REQUIRED BY THE DIRECTOR.

- 7 -

- D. F. In addition to the information required by subsection C E of this section each applicant captive insurer shall file with the director evidence of all of the following:
- 1. The amount and liquidity of its assets relative to the risks to be assumed.
- 2. The adequacy of the expertise, experience and character of the person or persons who will manage the captive insurer.
  - 3. The overall soundness of its plan of operation.
- 4. The adequacy of the loss prevention programs of its <del>parent or member organizations</del> INSUREDS.
  - 5. The engagement of a competent manager that resides in this state.
- 6. The establishment of business relationships with any necessary accountants, banks, attorneys and other professionals that do business at a location in this state.
- 7. The ability of the captive insurer's affiliates or association members OWNERS to pay claims to third parties if the captive insurer is unable to pay those claims.
- 8. Other factors deemed relevant by the director in ascertaining whether the proposed captive insurer will be able to meet its policy obligations.
- G. IN ADDITION TO THE INFORMATION REQUIRED BY SUBSECTIONS E AND F OF THIS SECTION, IF THE APPLICANT IS SEEKING AUTHORITY AS A PROTECTED CELL CAPTIVE INSURER, THE APPLICANT SHALL FILE:
- 1. A BUSINESS PLAN THAT DEMONSTRATES, IN A MANNER ACCEPTABLE TO THE DIRECTOR, HOW THE APPLICANT WILL ACCOUNT FOR THE LOSS AND EXPENSE EXPERIENCE OF EACH PROTECTED CELL AND REPORT THAT INFORMATION TO THE DIRECTOR.
- 2. A STATEMENT ACKNOWLEDGING THAT ALL FINANCIAL RECORDS OF THE PROTECTED CELL CAPTIVE INSURER, INCLUDING RECORDS PERTAINING TO PROTECTED CELLS, SHALL BE AVAILABLE FOR INSPECTION OR EXAMINATION BY THE DIRECTOR OR THE DIRECTOR'S DESIGNEE.
  - 3. ITS FORM FOR ALL PARTICIPANT CONTRACTS.
- 4. EVIDENCE THAT THE PROTECTED CELL CAPTIVE INSURER WILL ALLOCATE EXPENSES FAIRLY AND EQUITABLY TO EACH PROTECTED CELL.
- E. H. A captive insurer shall notify the director within thirty days of any material change in the information filed pursuant to this section.
- F. I. Notwithstanding title 39, chapter 1, information submitted pursuant to this section is confidential and the director and the director's employees and agents shall not provide the information to any other person without the written consent of the captive insurer, except that:
- 1. This section does not apply to the department's use of information submitted by a captive insurer for any regulatory purpose, disciplinary action or hearing.
- 2. The director shall provide information submitted by a captive insurer that is required by a subpoena issued in connection with an administrative, civil or criminal investigation by a government agency.

· 8 -

- 3. The information may be discoverable by a party in a civil action or contested case to which the captive insurer that submitted the information is a party, if the party seeking to discover the information demonstrates all of the following:
- (a) The information sought is relevant to and necessary for the furtherance of the action or case.
- (b) The information sought is unavailable from other nonconfidential sources.
- (c) A subpoena issued by a judicial or administrative officer of competent jurisdiction has been submitted to the director.
- 4. The director may disclose the information to a public official that has jurisdiction over the regulation of insurance in another state if the public official agrees in writing to maintain the confidentiality of the information and the laws of the state in which the public official serves allow or require the information to be and remain confidential.
- 5. The director may provide the information to the industrial commission. The industrial commission shall maintain the confidentiality of the information in accordance with this subsection.
- G. J. A captive insurer shall pay to the director a nonrefundable fee for the issuance and renewal of a captive insurance license pursuant to section 20-167. The captive insurer shall pay the renewal fee when the captive insurer files the annual report prescribed in section 20-1098.05 20-1098.07.
- H. K. If the director is satisfied that the documents and statements that the captive insurer has filed comply with this article, the director may grant the captive insurer a license that authorizes the captive insurer to transact insurance business in this state. If the plan of operation includes the reinsurance of workers' compensation or employers' liability risks resident, located or to be performed in this state, the director shall provide the industrial commission with an opportunity to review the plan of operation and advise the director as to its soundness.
- $\overline{\mbox{1.}}$  L. The director shall approve or deny an application for a license to transact captive insurance business within thirty days after the director deems the application complete.
- Sec. 4. Section 20-1098.03, Arizona Revised Statutes, is amended to read:

### 20-1098.03. Minimum capital and surplus: letter of credit

- A. The director shall not issue a license to a pure captive insurer or association captive insurer unless the insurer possesses and thereafter maintains minimum unimpaired paid-in capital and surplus in combination as follows:
- 1. In the case of a pure captive insurer, at least two hundred fifty thousand dollars.
- 2. In the case of an association A GROUP captive insurer, at least five hundred thousand dollars.

- 9 -

- 3. IN THE CASE OF AN AGENCY CAPTIVE INSURER, AT LEAST FIVE HUNDRED THOUSAND DOLLARS.
- 4. IN THE CASE OF A PROTECTED CELL CAPTIVE INSURER, AT LEAST ONE MILLION DOLLARS.
- 5. IN THE CASE OF A CAPTIVE INSURER THAT IS ORGANIZED AS A RECIPROCAL INSURER, AT LEAST FIVE HUNDRED THOUSAND DOLLARS IN FREE SURPLUS.
- 3. 6. In the case of a PURE OR GROUP captive insurer that transacts only reinsurance, one-half of the applicable amount prescribed in paragraph 1 or 2 of this subsection.
- B. All minimum capital and surplus requirements shall be in the form of CASH OR an irrevocable and unconditional letter of credit that contains an evergreen clause, that is payable to, filed with and held by the director in trust for the protection of all policyholders, ceding insurers and related expenses and that meets the following conditions:
- 1. The letter of credit shall be issued or confirmed by a qualified United States financial institution as defined in section 20-261.03, subsection A and shall comply with the requirements prescribed by the director.
- 2. The captive insurer shall not be directly or contingently liable for any letter of credit comprising its capital or surplus and its assets shall not be pledged as security for the letter of credit.
- C. The director may prescribe additional capital and surplus requirements based on the type, volume and nature of insurance.
- Sec. 5. Section 20-1098.04, Arizona Revised Statutes, is amended to read:

#### 20-1098.04. Formation of captive insurers; redomestication

- A. A pure captive insurer, AGENCY CAPTIVE INSURER OR PROTECTED CELL CAPTIVE INSURER shall be incorporated as a stock insurer with its capital divided into shares and held by the stockholders.
- $\ensuremath{\text{B.}}$  An association A GROUP captive insurer may be formed in any of the following ways:
- 1. Incorporated as a stock insurer with its capital divided into shares and held by the stockholders.
- 2. Incorporated as a mutual insurer without capital stock, the governing body of which is elected by the member organizations of its association.
- 3. ORGANIZED AS A RECIPROCAL INSURER PURSUANT TO ARTICLE 2 OF THIS CHAPTER.
- C. EACH OWNER OF AN AGENCY CAPTIVE INSURER SHALL BE LICENSED AS AN INSURANCE PRODUCER OR MANAGING GENERAL AGENT.
- C. D. A captive insurer shall have at least three incorporators at least one of whom shall be a resident of this state.
- D. E. The capital stock of a captive insurer incorporated as a stock insurer may be authorized with no par value.

- 10 -

- E. A captive insurer that is formed as a corporation has the privileges prescribed in and is subject to the applicable provisions of title 10 and the applicable provisions contained in this article. The provisions of article 1 of this chapter relating to mergers, consolidations, conversions, mutualizations and redomestications apply in determining the procedures to be followed by captive insurers in carrying out those transactions, except that the director may waive or modify the requirements for a public notice and hearing prescribed in section 20-731.
- F. The articles of incorporation or bylaws of a captive insurer that is formed as a corporation may authorize a quorum of a board of directors to consist of at least one-third of the fixed or prescribed number of directors. THE SUBSCRIBERS' AGREEMENT OR OTHER ORGANIZING DOCUMENT OF A CAPTIVE INSURER FORMED AS A RECIPROCAL INSURER MAY AUTHORIZE A QUORUM OF A SUBSCRIBERS' ADVISORY COMMITTEE TO CONSIST OF AT LEAST ONE-THIRD OF THE NUMBER OF ITS MEMBERS.
- G. A CAPTIVE INSURER ORGANIZED AS A STOCK INSURER SHALL HAVE AT LEAST ONE MEMBER OF THE BOARD OF DIRECTORS WHO IS A RESIDENT OF THIS STATE. A CAPTIVE INSURER THAT IS FORMED AS A RECIPROCAL INSURER SHALL HAVE AT LEAST ONE MEMBER OF THE SUBSCRIBERS' ADVISORY COMMITTEE WHO IS A RESIDENT OF THIS STATE.
- H. ANY FOREIGN OR ALIEN INSURER MAY BECOME A DOMESTIC CAPTIVE INSURER BY COMPLYING WITH THE REQUIREMENTS OF THIS ARTICLE RELATING TO THE ORGANIZATION AND LICENSING OF A DOMESTIC CAPTIVE INSURER OF THE SAME TYPE, AND BY COMPLYING WITH ALL APPLICABLE REQUIREMENTS OF THE LAWS OF THIS STATE RELATING TO THE FORMATION AND AUTHORIZATION OF A CORPORATION. THE DOMESTIC CAPTIVE INSURER IS ENTITLED TO A LICENSE TO CONTINUE ITS BUSINESS AND IS SUBJECT TO THE AUTHORITY AND JURISDICTION OF THIS STATE.

#### Sec. 6. Renumber

Sections 20-1098.05 through 20-1098.15, Arizona Revised Statutes, are renumbered as sections 20-1098.07 through 20-1098.17, respectively.

Sec. 7. Title 20, chapter 4, article 14, Arizona Revised Statutes, is amended by adding sections 20-1098.05 and 20-1098.06, to read:

20-1098.05. Protected cell captive insurers

- A. ONE OR MORE SPONSORS MAY FORM A PROTECTED CELL CAPTIVE INSURER AS PRESCRIBED IN THIS ARTICLE.
- B. A PROTECTED CELL CAPTIVE INSURER MAY ESTABLISH AND MAINTAIN ONE OR MORE PROTECTED CELLS TO INSURE THE RISKS OF ONE OR MORE PARTICIPANTS, SUBJECT TO THE FOLLOWING CONDITIONS:
- 1. A PROTECTED CELL CAPTIVE INSURER SHALL NOT HAVE ANY STOCKHOLDERS OTHER THAN ITS PARTICIPANTS AND SPONSORS.
- 2. A PROTECTED CELL CAPTIVE INSURER SHALL SEPARATELY ACCOUNT FOR EACH PROTECTED CELL IN ITS BOOKS AND RECORDS TO REFLECT THE FINANCIAL CONDITION AND RESULTS OF OPERATIONS OF EACH PROTECTED CELL, NET INCOME OR LOSS OF EACH PROTECTED CELL, DIVIDENDS OR OTHER DISTRIBUTIONS TO PARTICIPANTS OF EACH

- 11 -

 PROTECTED CELL AND ANY OTHER FACTORS PRESCRIBED IN THE PARTICIPANT CONTRACT OR REQUIRED BY THE DIRECTOR.

- 3. THE ASSETS OF A PROTECTED CELL ARE NOT CHARGEABLE WITH LIABILITIES ARISING OUT OF ANY OTHER INSURANCE BUSINESS THE PROTECTED CELL CAPTIVE INSURER MAY CONDUCT.
- 4. A PROTECTED CELL CAPTIVE INSURER SHALL NOT SELL, EXCHANGE OR TRANSFER ASSETS, ISSUE A DIVIDEND OR MAKE A DISTRIBUTION BETWEEN OR AMONG ANY OF ITS PROTECTED CELLS WITHOUT THE WRITTEN CONSENT OF ALL ITS PROTECTED CELLS.
- 5. A PROTECTED CELL CAPTIVE INSURER SHALL NOT SELL, EXCHANGE OR TRANSFER ASSETS, ISSUE A DIVIDEND OR MAKE A DISTRIBUTION TO A SPONSOR OR PARTICIPANT UNLESS THE DIRECTOR APPROVES THE TRANSACTION AND DETERMINES THAT THE TRANSACTION WILL NOT CAUSE INSOLVENCY OR IMPAIRMENT OF ANY PROTECTED CELL.
- 6. AT THE TIME OF FILING ITS ANNUAL REPORT PURSUANT TO SECTION 20-1098.07 A PROTECTED CELL CAPTIVE INSURER SHALL ANNUALLY FILE WITH THE DEPARTMENT:
- (a) AN ACCOUNTING STATEMENT, IN THE FORM THE DIRECTOR REQUIRES, DETAILING THE FINANCIAL EXPERIENCE OF EACH PROTECTED CELL.
  - (b) ANY OTHER FINANCIAL REPORTS PRESCRIBED BY THE DIRECTOR.
- 7. A PROTECTED CELL CAPTIVE INSURER SHALL NOTIFY THE DIRECTOR IN WRITING WITHIN TEN DAYS AFTER LEARNING OF ANY PROTECTED CELL THAT IS INSOLVENT OR OTHERWISE UNABLE TO MEET ITS CLAIM OR EXPENSE OBLIGATIONS.
- 8. A PROTECTED CELL CAPTIVE INSURER SHALL OBTAIN THE DIRECTOR'S WRITTEN APPROVAL OF ANY PARTICIPANT CONTRACT BEFORE THE CONTRACT BECOMES EFFECTIVE.
- 9. THE ADDITION OF A NEW PARTICIPANT OR THE WITHDRAWAL OF A PARTICIPANT FROM AN EXISTING PROTECTED CELL IS DEEMED A CHANGE IN THE CAPTIVE INSURER'S BUSINESS PLAN AND REQUIRES THE DIRECTOR'S PRIOR APPROVAL.
- 10. WITH RESPECT TO EACH PROTECTED CELL, THE INSURANCE BUSINESS WRITTEN BY A PROTECTED CELL CAPTIVE INSURER SHALL BE:
- (a) ASSUMED FROM AN INSURANCE COMPANY LICENSED UNDER THE LAWS OF ANY STATE.
  - (b) REINSURED BY A REINSURER AUTHORIZED OR ACCREDITED BY THIS STATE.
- (c) SECURED BY A TRUST FUND OR AN IRREVOCABLE LETTER OF CREDIT WITH AN EVERGREEN CLAUSE.

20-1098.06. <u>Protected cell captive insurers; sponsors;</u> participants

A. A SPONSOR OF A PROTECTED CELL CAPTIVE INSURER SHALL BE A FOREIGN OR DOMESTIC INSURER, A REINSURER AUTHORIZED OR APPROVED UNDER THE LAWS OF ANY STATE OR A CAPTIVE INSURER FORMED OR LICENSED UNDER THIS ARTICLE. A RISK RETENTION GROUP SHALL NOT BE EITHER A SPONSOR OR A PARTICIPANT IN A PROTECTED CELL CAPTIVE INSURER.

- 12 -

- B. AN ASSOCIATION, CORPORATION, LIMITED LIABILITY COMPANY, PARTNERSHIP, TRUST OR ANY OTHER BUSINESS ENTITY MAY BE A PARTICIPANT IN ANY PROTECTED CELL CAPTIVE INSURER FORMED OR LICENSED UNDER THIS ARTICLE.
  - C. A SPONSOR MAY BE A PARTICIPANT IN A PROTECTED CELL CAPTIVE INSURER.
- D. A PARTICIPANT NEED NOT BE A SHAREHOLDER OF A PROTECTED CELL CAPTIVE INSURER OR ANY AFFILIATE OF A PROTECTED CELL CAPTIVE INSURER.
- E. A PARTICIPANT SHALL INSURE ONLY ITS OWN RISKS THROUGH A PROTECTED CELL CAPTIVE INSURER.
- Sec. 8. Section 20-1098.07, Arizona Revised Statutes, as renumbered by this act, is amended to read:

#### 20-1098.07. <u>Annual report</u>

- A. Not later than ninety days after the end of the captive insurer's fiscal year, the captive insurer shall submit to the director a report of its financial condition that is verified by oath of two of its executive officers and that is supplemented by additional information as required by the director. Except as provided in section 20-1098.03, a captive insurer may submit a report that uses generally accepted accounting principles unless the director requires the captive insurer to use statutory accounting principles with any useful or necessary modifications or adaptations of those principles required by the director for the type of insurance and kinds of insurers to be reported on.
- B. The captive insurer's financial statements shall be audited by an independent certified public accountant unless the director determines that an audit is not necessary. THE AUDIT SHALL INCLUDE AN OPINION AS TO THE ADEQUACY OF THE CAPTIVE INSURER'S LOSS RESERVES AND LOSS EXPENSE RESERVES.
- Sec. 9. Section 20-1098.08, Arizona Revised Statutes, as renumbered by this act, is amended to read:

#### 20-1098.08 Examinations

- A. Whenever the director determines it to be prudent, the director may examine the business, transactions and affairs of each captive insurer to ascertain the captive insurer's financial condition and ability to fulfill its obligations and whether the captive insurer has complied with this article.
- B. Section 20-1098.01, subsection  $\digamma$  I applies to all examination reports, preliminary examination reports or results, working papers, recorded information, documents and copies of any of those reports, results, papers, information or documents produced by, obtained by or disclosed to the director in the course of an examination made under this section.
- C. The director may use independent contractor examiners pursuant to sections 20-148 and 20-159 to conduct examinations pursuant to this section. All examinations and examination related expenses shall be borne by the captive insurer and shall be paid by the insurance examiners' revolving fund pursuant to section 20-159.

- 13 -

Sec. 10. Section 20–1098.09, Arizona Revised Statutes, as renumbered by this act, is amended to read:

## 20-1098.09. <u>Grounds and procedures for license suspension or revocation</u>

The director may suspend, revoke or refuse to renew the license of a captive insurer to transact insurance business in this state for any of the following reasons:

- Insolvency or impairment of capital and surplus.
- 2. Refusal or failure to submit an annual report as prescribed in section 20-1098.05 20-1098.07 or any other report or statement required by law or by lawful order of the director.
- 3. Failure to comply with the provisions of its own articles of incorporation, bylaws or other organizational document.
- 4. Failure to submit to an examination or any legal obligation related to the examination as prescribed in section <del>20-1098.06</del> 20-1098.08.
- 5. Refusal or failure to pay the cost of an examination as prescribed in section 20-1098.06 20-1098.08.
- 6. Use of methods that, although not otherwise specifically prohibited by law, render its operation hazardous or its condition unsound with respect to the public or to its policyholders.
  - 7. Failure to otherwise comply with this article.
- Sec. 11. Section 20-1098.10, Arizona Revised Statutes, as renumbered by this act, is amended to read:

#### 20-1098.10. Legal investments

- A. An association A GROUP captive insurer, AN AGENCY CAPTIVE INSURER AND A PROTECTED CELL CAPTIVE INSURER shall comply with the investment requirements prescribed in chapter 3, article 2 of this title. Notwithstanding any other provision of this title, the director may approve the use of alternative reliable methods of valuation and rating.
- B. A pure captive insurer is not subject to restrictions on allowable investments, except that the director may prohibit or limit any investment that threatens the solvency or liquidity of the pure captive insurer.
- C. Only a pure captive insurer may make loans to its affiliates if before making a loan to an affiliate the pure captive insurer obtains written approval by the director to make the loan and the loan is evidenced by a note in a form approved by the director. A NOTE SHALL EVIDENCE THE LOAN. BEFORE MAKING ANY SUCH LOAN, THE PURE CAPTIVE INSURER SHALL OBTAIN THE DIRECTOR'S WRITTEN APPROVAL TO MAKE THE LOAN AND APPROVAL FOR THE FORM OF THE NOTE.
- Sec. 12. Section 20-1098.13, Arizona Revised Statutes, as renumbered by this act, is amended to read:

20-1098.13. Associations: benefits: prohibitions

EXCEPT AS OTHERWISE PROVIDED IN SECTION 20-1098.01, SUBSECTION B FOR A SELF-INSURANCE PROGRAM APPROVED UNDER SECTION 23-961, a captive insurer shall not join or contribute financially to any plan, pool, association or guaranty or insolvency fund in this state. A captive insurer or its insured,

- 14 -

 A parent, AN affiliate, GROUP MEMBERS, A member organization of its AN association or A claimant under any captive insurance shall not receive any benefit from the plan, pool, association, or guaranty or insolvency fund for claims arising out of the operations of the captive insurer.

Sec. 13. Section 20-1098.15, Arizona Revised Statutes, as renumbered by this act, is amended to read:

20-1098.15. Applicability

- A. Chapter 2, article 6 of this title relating to unfair trade practices and frauds applies to captive insurers, except to the extent the director determines the nature of captive insurance renders particular portions of chapter 2, article 6 of this title inappropriate.
- B. All other provisions of this title that are not inconsistent with this article apply to captive insurers except to the extent the director determines the nature of captive insurance renders particular provisions of this title inappropriate.
- C. A CAPTIVE INSURER THAT IS FORMED AS A CORPORATION IS SUBJECT TO THE APPLICABLE PROVISIONS OF TITLE 10 EXCEPT AS OTHERWISE PRESCRIBED IN THIS ARTICLE.
- D. THE PROVISIONS OF ARTICLE 1 OF THIS CHAPTER RELATING TO MERGERS, CONSOLIDATIONS, CONVERSIONS, MUTUALIZATIONS AND REDOMESTICATIONS APPLY IN DETERMINING THE PROCEDURES TO BE FOLLOWED BY CAPTIVE INSURERS IN CARRYING OUT THOSE TRANSACTIONS, EXCEPT THAT THE DIRECTOR MAY WAIVE OR MODIFY THE REQUIREMENTS FOR A PUBLIC NOTICE AND HEARING PRESCRIBED IN SECTION 20-731.
- Sec. 14. Title 20, chapter 4, article 14, Arizona Revised Statutes, is amended by adding section 20-1098.18, to read:

# 20-1098.18. <u>Captive insurance regulatory and supervision fund;</u> <u>purpose</u>

- A. THE CAPTIVE INSURANCE REGULATORY AND SUPERVISION FUND IS ESTABLISHED WITHIN THE DEPARTMENT CONSISTING OF MONIES DEPOSITED PURSUANT TO SECTION 20-1098.01, SUBSECTION J. THE DIRECTOR SHALL ADMINISTER THE FUND AS PRESCRIBED IN SUBSECTION B OF THIS SECTION. MONIES IN THE FUND ARE EXEMPT FROM THE PROVISIONS OF SECTION 35-190 RELATING TO LAPSING OF APPROPRIATIONS, EXCEPT THAT, ON THE CLOSE OF EACH FISCAL YEAR, ALL UNENCUMBERED MONIES IN THE FUND EXCEEDING ONE HUNDRED THOUSAND DOLLARS REVERT TO THE STATE GENERAL FUND.
- B. THE DIRECTOR SHALL USE MONIES IN THE CAPTIVE INSURANCE REGULATORY AND SUPERVISION FUND TO PAY THE COSTS OF ADMINISTERING THIS ARTICLE AND FOR REASONABLE EXPENSES INCURRED IN PROMOTING THIS STATE'S CAPTIVE INSURANCE INDUSTRY.
- C. THE DEPARTMENT SHALL NOT RECEIVE A GENERAL FUND APPROPRIATION FOR OPERATION OF THE CAPTIVE INSURANCE PROGRAM AND PROMOTION OF THIS STATE'S CAPTIVE INSURANCE INDUSTRY FOR ANY FISCAL YEAR IN WHICH THE DEPARTMENT HAD AT LEAST TWENTY-FIVE CAPTIVE INSURERS HOLDING AN ACTIVE CERTIFICATE OF AUTHORITY AS OF THE IMMEDIATELY PRECEDING CALENDAR YEAR END.

APPROVED BY THE GOVERNOR MAY 20, 2003

FILED IN THE OFF. OF THE SECRETARY OF STATE MAY 21, 2003.

Passed the House	Passed the Senate	April 8,2	0_03
by the following vote: 59 Ayes,	by the following vote: _	30	_Ayes,
Nays, Not Voting  Ale Speaker of the House  Horman J. Motre  Chief Clerk of the House	Lili	Resident of the Senate Secretary of the Senate	t Voting
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Governor of Arizona			,
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		was received by the Secretary	of State
Н.В. 2152	this	day of,	20,
	at	o'clock	M.

Secretary of State

HOUSE FINAL PASSAGE as per Joint Conference	SENATE FINAL PASSAGE as per Joint Conference
Passed the House May 7, 2003,	Passed the Senate May 13, 2003,
by the following vote: 55 Ayes,	by the following vote: 27 Ayes,
Nays, 5 Not Voting	Nays, 3 Not Voting
Speaker of the House	President of the Senate
Chief Clerk of the House	Secretary of the Senate
OFFICE OF This Bill was receing this day of at at at at at at at at at	TMENT OF ARIZONA F GOVERNOR ved by the Governor  o'clock M.  ecretary to the Governor
Approved this day of	
Governor of Arizona	EXECUTIVE DEPARTMENT OF ARIZONA OFFICE OF SECRETARY OF STATE
	This Bill was received by the Secretary of State
	this
H.B. 2152	at 3:56 o'clock 7. M.
	Secretary of State